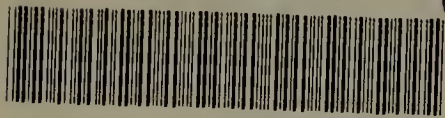


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The Governor's Message

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Fiscal Year 1999

Budget Recommendation



Commonwealth of Massachusetts

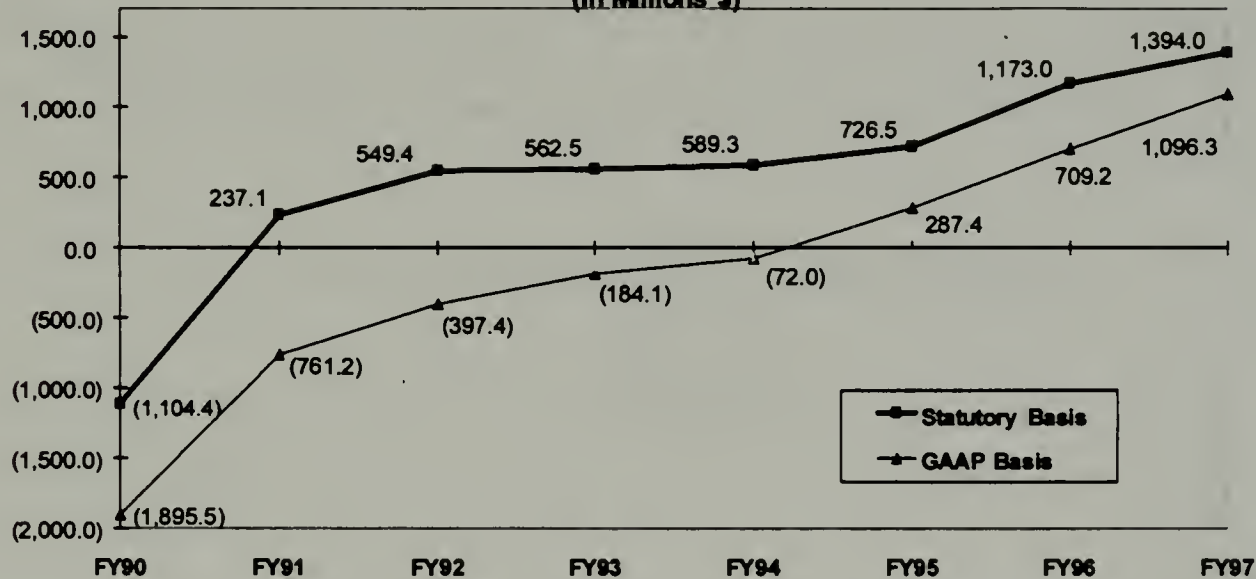
Argeo Paul Cellucci, Governor

A Message From Governor Argeo Paul Cellucci

Introduction

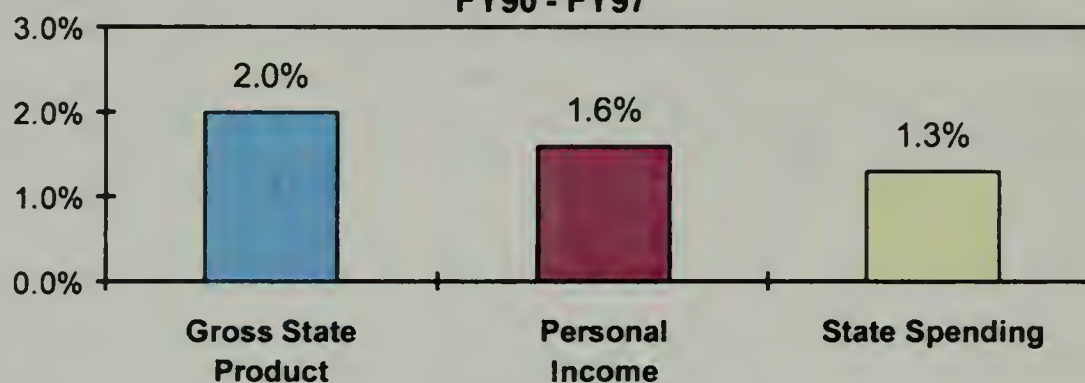
When former-Governor Weld and I took Office in 1991, we inherited a \$1.9 billion dollar deficit according to GAAP or generally accepted accounting principles. Since that time, this Administration has made enormous progress in restoring fiscal balance. In fact, the Massachusetts Comptroller just released the Fiscal Year 1997 Comprehensive Annual Financial Report for the Commonwealth of Massachusetts which indicates that the Commonwealth closed Fiscal Year 1997 with a positive GAAP balance of \$1.1 billion (see Chart #1).

Chart #1
Trends in Budgeted Funds Balance
FY90 - FY97
(in Millions \$)



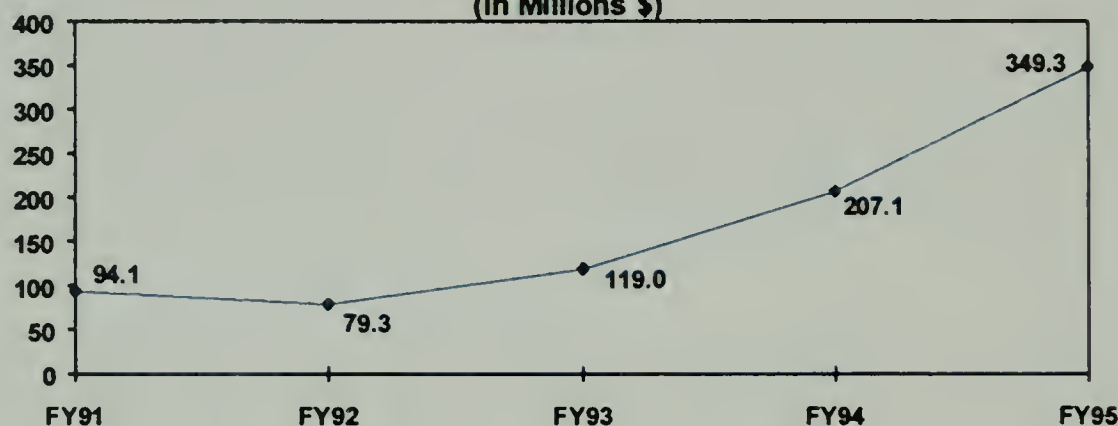
The Comptroller attributes this \$3 billion swing in fund balances to several things, but mentions, in particular, prudent fiscal management characterized by structurally balanced budgets. This Administration has never lived beyond its means. Since 1991, state spending has grown more slowly than the growth in available revenue, personal income, and Gross State Product; and the growth in Executive Branch spending has been at or below the rate of inflation. As a result, we have contributed almost \$800 million to a Stabilization Fund that was empty when we took office, and improved our bond rating from just short of junk bond status to a respectable AA- (see Chart #2).

Chart #2
Annual Growth Rate in Dollars
Adjusted for Inflation
FY90 - FY97



At the same time, we worked diligently to ensure the fiscal health of the Commonwealth's cities and towns by phasing out any state claim to Lottery profits, and by pouring over \$2.8 billion into K-12 education reform. By 1995, city and town "certified free cash balances" had rebounded to over \$350 million, and today, city and town balance sheets have never looked better (see Chart #3).

Chart #3
Municipal Certified "Free Cash" Balance Totals
Summary
FY91 - FY95
(in Millions \$)



Finally, we pursued an aggressive tax-cutting agenda which has resulted in the enactment of 21 tax cuts over the past seven years, worth more than \$1.2 billion in savings to Massachusetts taxpayers.

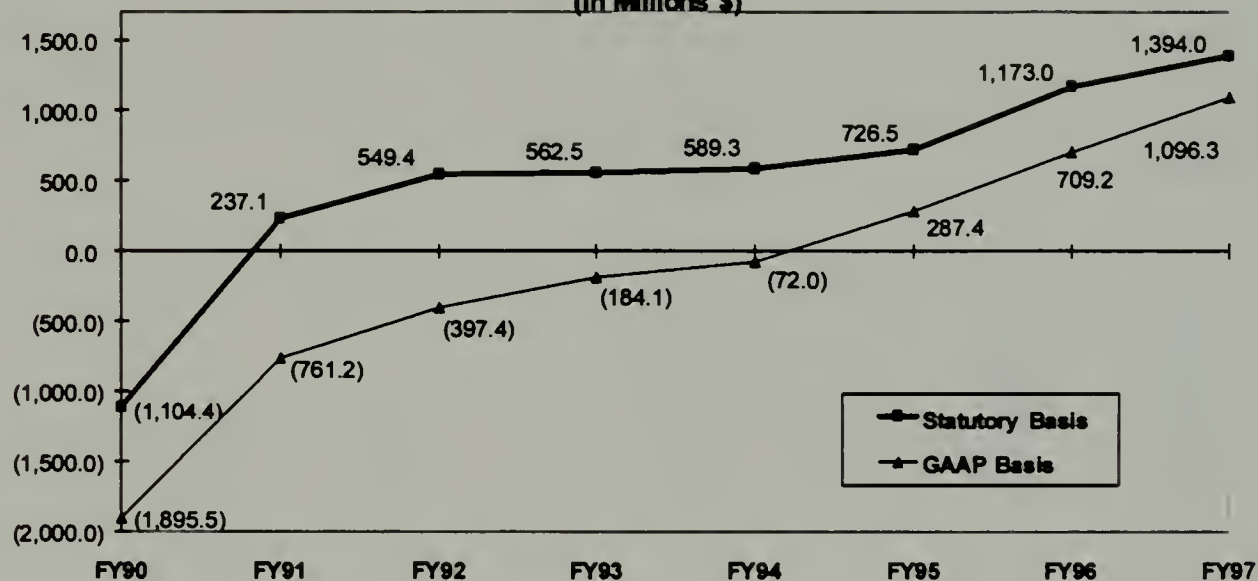
Our economy has responded favorably to this combination of fiscal discipline and tax reductions. In 1991, we had one of the highest unemployment rates in the country - 9.6%. For the past year, our unemployment rate has remained at or below 4%, significantly below the national average. The Massachusetts economy has created over 360,000 net new jobs since 1991, and manufacturing employment for the past year is up by almost 2% - the largest annual increase in manufacturing employment in over 12 years.

A Message From Governor Argeo Paul Cellucci

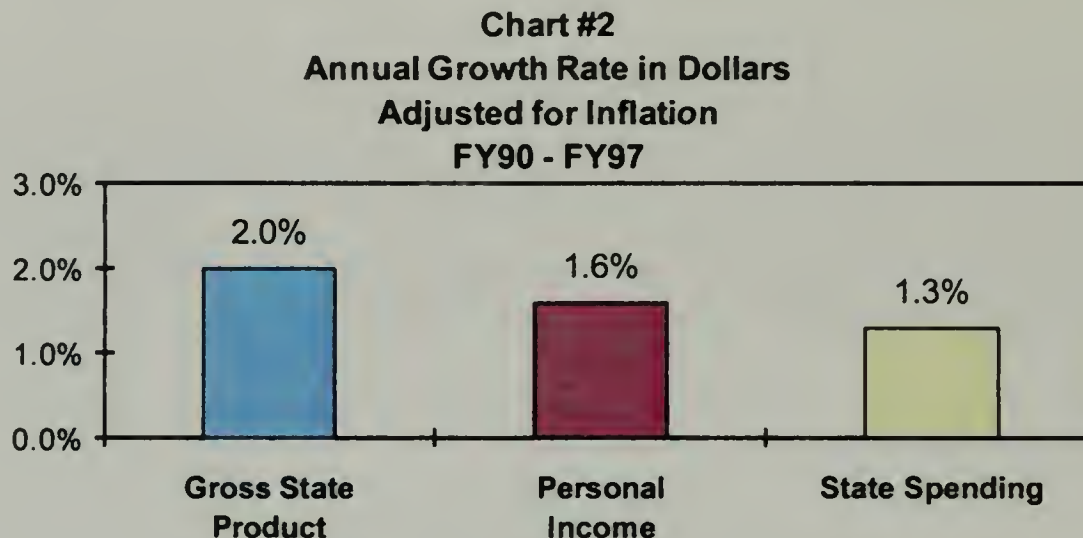
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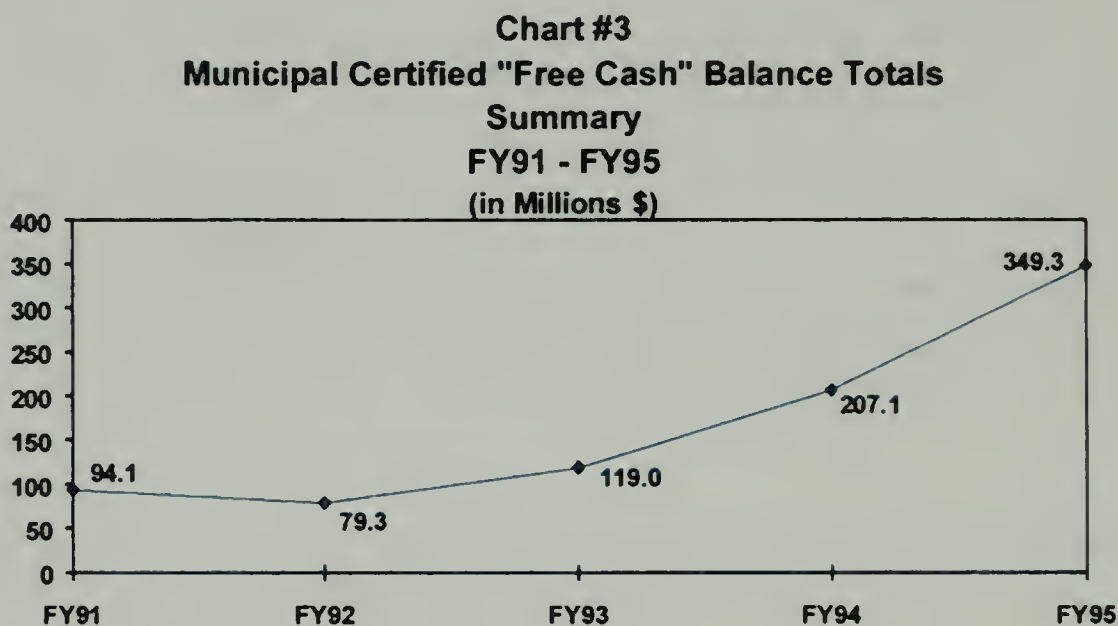
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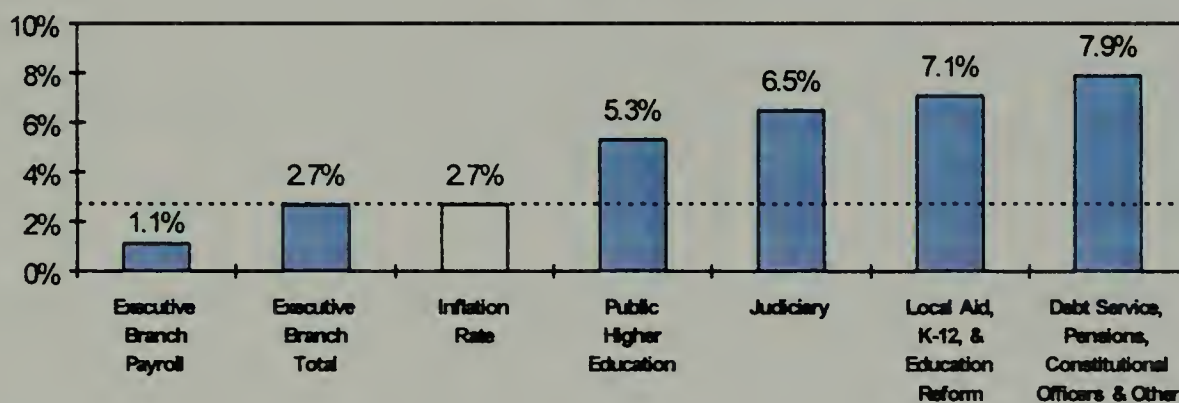
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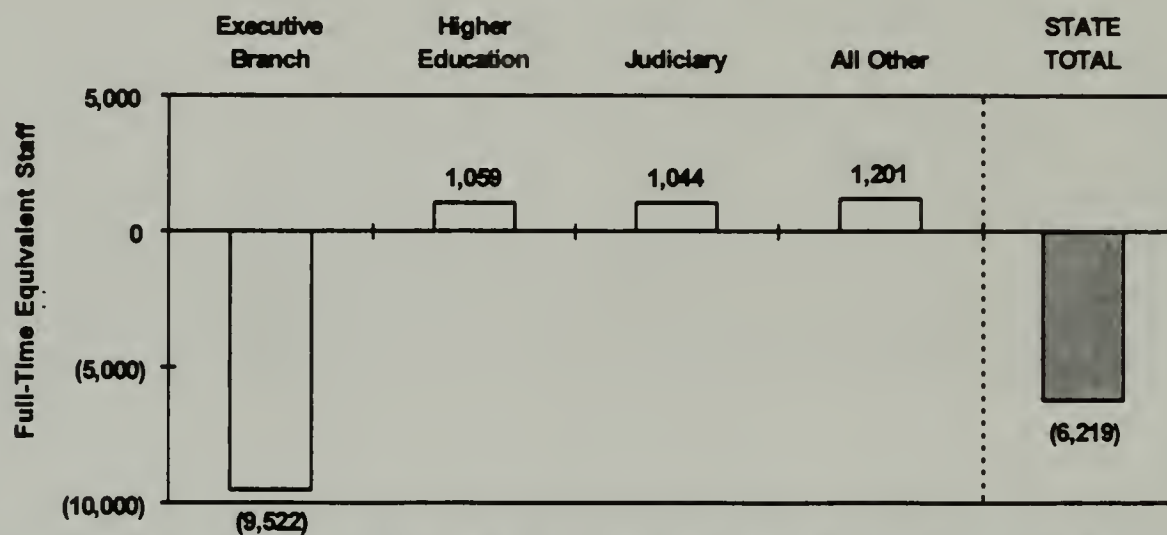
Fiscal Year 1998 Overview

The current fiscal year is simply more of the same medicine. The vast majority of the increase in state spending in Fiscal Year 1998 will fund education reform and the continued phase-out of the cap on Lottery aid distribution to cities and towns. The criminal justice system continues to receive generous support from the Commonwealth, we continue to pay down the unfunded pension liability we inherited when we took office, and tuitions and fees continue to be reduced at public higher education institutions as state support climbs. In fact, by dramatically reducing the size of the Executive Branch workforce and by limiting the growth in Executive Branch spending to the rate of inflation for the past seven years, we have made it possible to fund enormous increases in local aid to cities and towns, various criminal justice initiatives, including expansion of the Juvenile Court system, generous increases in state support for public higher education, and significant progress on fully funding our public pension system (see Charts #4 & #5).

Chart #4
Annual Increase in Spending
Relative to Inflation
1991 - 1997



**Chart #5
State Workforce*
Change Since 1991**



* Full-time equivalent filled standard workforce positions active on payroll

In addition, we completed the transition of Middlesex and Franklin Counties into state government earlier this year. Franklin County chose to join the Commonwealth during Fiscal Year 1996, and we worked with them to pursue an orderly transition. In Fiscal Year 1997, Middlesex County, on the other hand, simply spent itself into bankruptcy, forcing the Commonwealth to pick up the pieces and put its component parts back together again. In Fiscal Year 1999, Worcester and Hampden Counties will be the next two counties to make an orderly transition into state government.

We also made a significant change in our corporate sales tax collection policy. Under the previous policy, most Massachusetts retailers were required to file state sales tax reports sixteen times per year: once per month on an estimated basis, and then four times a year to reconcile actual collections to estimates. It was an unnecessarily complex and administratively burdensome process, for retailers and for the Commonwealth.

Starting this month, we will collect actual sales tax receipts 30 days after the taxes are paid to retailers. This adjustment will reduce tax receipts to the Commonwealth by \$140 million on a one-time basis during Fiscal Year 1998, but will save the retailing community hours and hours of wasted time and energy spent trying to comply with the previous policy, and make compliance monitoring efforts on our part far easier to execute.

As a final issue, we fund the Health Care Access Act of 1996 for the first time in Fiscal Year 1998. Since the start of this fiscal year, I am proud to point out that we have enrolled over 75,000 new beneficiaries into our expanded Medicaid program. President Clinton has recently expressed concerns about the ability of state and federal governments to reach out to newly eligible populations. Our success in reaching and enrolling new populations in this program is a model for the nation.

Fiscal Year 1999

The debate about the Fiscal Year 1999 budget should begin and end with an honest and open discussion about cutting taxes. Prudent financial management and a rock solid economy have produced a budgetary surplus that would have been considered impossible just a few short years ago. More importantly, when state policymakers decided to raise income tax rates in 1990, they said the increase would be "temporary." They said the state would raise income tax rates to fund bonds that would be sold to pay off the operating deficits of the 1980's, but the state would restore the old income tax rate once the bonds were paid off.

Seven years later, we have paid these bonds. Now it is time to reduce the personal income tax from 5.95% to its original rate of 5%. We propose to do this over three calendar years. Given our current financial condition, this is an eminently manageable proposal.

We also propose to reduce the income tax on interest and dividends from 12% to 5% over five fiscal years. Massachusetts is the only state in the country that taxes regular income and interest income differently. This depresses investment and discourages savings. Almost 90% of the people who will benefit from this tax change earn less than \$100,000 per year. Over 60% earn less than \$50,000.

To provide Massachusetts residents with access to the full value of several recent federal tax law changes and to ensure access to higher education for working families, I am proposing three additional changes to Massachusetts tax law. First, to encourage Massachusetts parents to begin saving money now for their children's higher education costs, I am proposing a 5% personal income tax credit (capped at \$250 annually) for deposits in education IRA's or the Massachusetts College Investment Savings Program (MCISP). Second, I propose a tax exemption on earnings and withdrawals from the MCISP and education IRA's used for higher education tuition, fees, room, and board. Finally, I propose a state tax deferral for income earnings from new "Roth" IRA's.

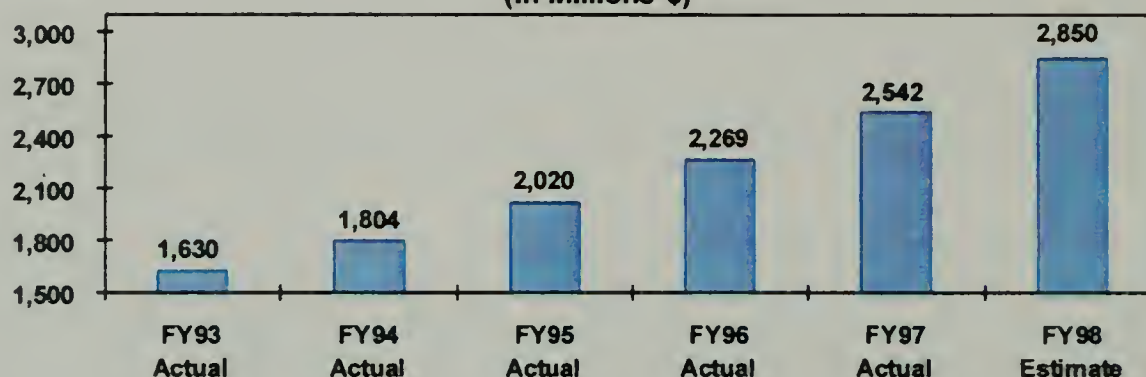
The time to act on these initiatives is now. The Commonwealth of Massachusetts is awash with money, but it is the taxpayers' money, not the government's. We owe the people of Massachusetts a reduction in their income tax, and other taxes, such as our tax rate on interest and dividend income which remains punitively high and economically destructive. We have worked with the Legislature to deliver \$1.2 billion in annual tax savings to Massachusetts taxpayers over the past seven years. Our efforts have been rewarded with an ever-expanding state economy. Now we have an opportunity to thank the people of Massachusetts for their hard work and trust. We must not let this golden opportunity to make Massachusetts even more competitive in the years ahead slip away from us.

Making Education A Priority

During the past five years, the Commonwealth of Massachusetts has increased its annual level of spending on K-12 education by \$1.2 billion (see Chart #6). To put this investment in perspective, it is larger than the increase in the annual net state cost of all of the previously

so-called "Budget Busters" (Debt Service, Medicaid, Insurance Costs, MBTA Subsidies, and Pensions) from Fiscal Year 1993 through Fiscal Year 1998. Since Fiscal Year 1993, the Commonwealth has allocated over \$13 billion to support K-12 education, more than it will spend to depress the Central Artery and build the Third Harbor Tunnel.

Chart #6
Total K-12 Spending
FY93 - FY98
(in Millions \$)



According to the Department of Education, local school systems have hired 8,500 new teachers over the past five years, and despite rising enrollments, have managed to reduce the average class size. Enormous inequities in funding between and among school districts have been virtually eliminated. The Department of Education (DOE) estimates that by the end of Fiscal Year 1999, 95% of all Massachusetts communities will be at or above 90% of their recommended level of spending per pupil (so-called "foundation funding"). In 1991, such a dramatic decline in funding inequality over such a short period of time would have been considered unattainable.

In Fiscal Year 1999, I am recommending \$269 million to fully fund the sixth year of Education Reform, but I am also proposing two significant modifications in funding for this important initiative. First, I will require local school districts to spend 90% of all new Chapter 70 money in the classroom, and not on unnecessary administration and overhead. This will assure parents and taxpayers that their hard-earned tax dollars will be spent primarily on hiring teachers and buying books. Second, I am increasing state support for K-12 education by another \$40 million over and above the state commitment to education reform, which will be allocated exclusively to hire new teachers and continue to reduce class size.

By themselves, these two initiatives will increase state support for schools in Fiscal Year 1999 by about \$309 million. This will make it possible for school districts across the Commonwealth to add 4,000 new teachers during the 1998/1999 school year, and continue to reduce class size and improve quality.

I am also recommending a \$15 million increase in early childhood education, targeted specifically to quality improvements, such as teacher certification, program accreditation, and facility repair and renovations. In Fiscal Year 1998, DOE allocated much of the new funding it received for early childhood education on similar efforts. We believe that this kind of capacity development is critical to the near and long-term success of all early childhood education and

child care initiatives. We are also proposing legislation, in an outside section to this budget, that requires the Department to collect more information on the children it is currently serving, and requiring DOE to work more closely with Health and Human Services on its quality and service initiatives.

Overall, I am recommending a \$55 million increase in early childhood education and child care spending.

In higher education, I am recommending an \$8 million reserve at the Board of Higher Education for the performance improvement program. This is a 33% increase over Fiscal Year 1998. I am also recommending an \$8 million increase in state funding for scholarships and a \$2 million matching grant program for Community Colleges, which can be leveraged with private contributions to support new programs in Adult Education. If we believe that working people should have the opportunity to continue to advance their educational achievement, we must be willing to support their endeavors.

A Special Initiative For At-Risk Youth

Between 1995 and 2005, the adolescent population in Massachusetts will grow by 25%. If we choose to act now to develop coordinated programs and services that are targeted to at-risk kids in at-risk neighborhoods, we can help many of these children avoid the kinds of problems that tend to overwhelm them once they reach adolescence. Therefore, I am directing Executive Office of Health and Human Services (EOHHS) Secretary William O'Leary to work with mayors and key community leaders across Massachusetts to develop a comprehensive plan for combating youth violence and delinquency in high-risk neighborhoods. I am particularly interested in developing programs and other support activities that focus on weekday afternoons between the hours of 2:00 p.m. and 6:00 p.m. when parents are at work and kids are not in school, and targeting discrete neighborhoods in our cities, where about half of all juvenile crime and violence occurs.

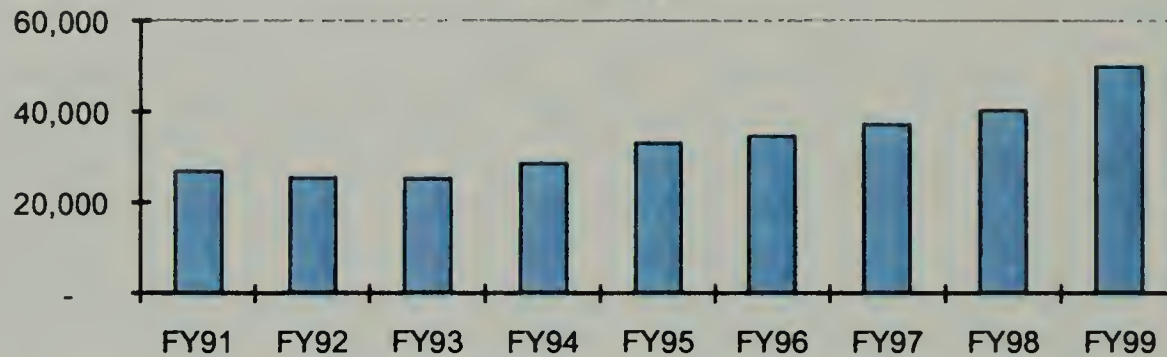
To support this initiative, I am recommending a \$3 million reserve at EOHHS, and I am proposing a \$5 million investment in after-school programming at the Department of Education, which will be coordinated with the Executive Office of Health and Human Services, other departments within EOHHS, and local agencies and providers to serve at-risk kids in designated neighborhoods across Massachusetts. We have discussed this idea with several mayors already, and they have encouraged us to pursue it further.

Health and Human Services

As Massachusetts continues to implement one of the most comprehensive welfare reform programs in the nation, we must be willing to support parents with child care and health care benefits as they enter the workforce. I am recommending an \$18 million increase in spending to support child care services for women transitioning off of welfare and into work. I am also proposing a \$10 million increase in state spending for income-eligible child care services, which is targeted directly toward the waiting list for early childhood education and child care

services compiled this past summer by the Office of Child Care Services. Overall, this budget is recommending an increase of more than \$40 million in spending on these services (See Chart #7).

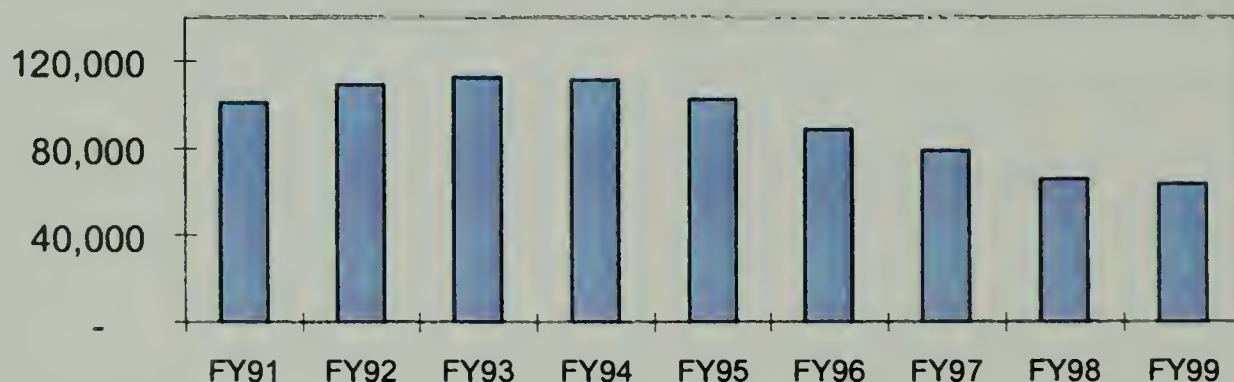
Chart #7
Subsidized Child Care Slots *
FY91-FY99



* Does not include child care spending at Department of Education

In Fiscal Year 1999, the first group of individuals currently receiving Transitional Aid to Families with Dependent Children (TAFDC) benefits will face their two year time limit and the loss of these benefits. Since passage of the state welfare reform legislation, the vast majority of individuals receiving these benefits who have left public assistance have successfully worked with the Department of Transitional Assistance (DTA) to gain the necessary skills to move into the workforce. Federal Welfare-to-Work funding administered by the Department of Labor and Workforce Development will further support DTA's efforts to provide job training and better prepare TAFDC recipients for work. However, a small group continues to face multiple barriers to employment. To help these individuals make a successful transition to work before their benefits end, I am recommending the Executive Office of Health and Human Services coordinate a multi-agency initiative to identify human service programs that will provide mental health, substance abuse, and other social services. I am also recommending an additional \$3 million at DTA for transportation, and expanded support programs to assist in reducing the barriers these individuals face in becoming self-sufficient (see Chart #8).

Chart #8
Declining TAFDC Caseloads
FY91-FY99



I am also proposing a \$4 million expansion within EOHHS for domestic violence prevention and intervention programs in addition to \$1.5 million in the Judiciary, Department of Education,

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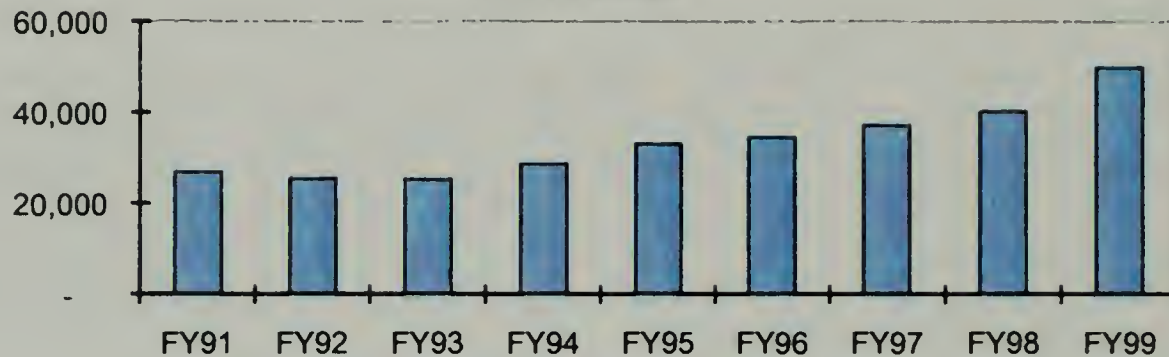
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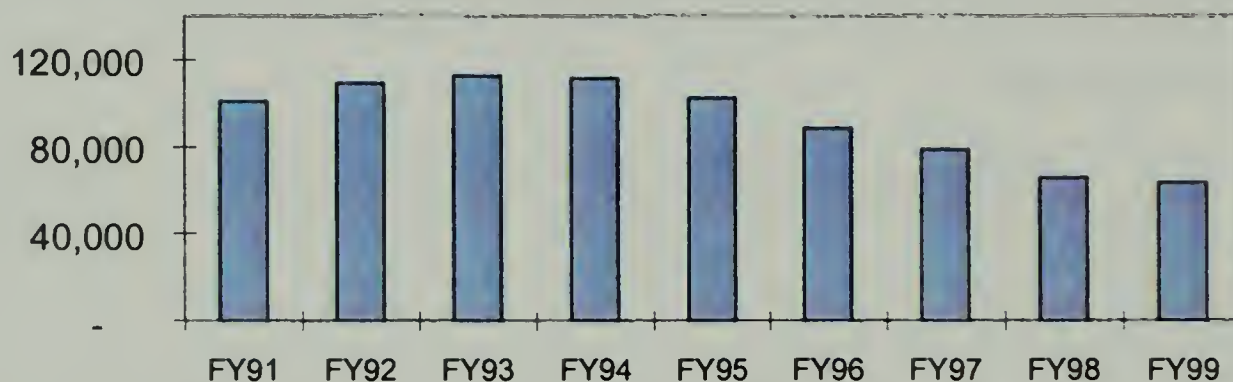
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and the District Attorneys. This will fund a \$2.2 million increase in existing programs such as the Batterer Intervention program, counseling services, and Visitation Centers, and will provide \$1.8 million for several new initiatives including a Child Witness program to protect and counsel children who witness domestic violence; a transitional housing program offering longer-term shelter for victims of domestic violence; and advocacy for non-English speaking victims.

Additionally, I am proposing that the Commonwealth take over direct management and administration of the Supplemental Security Income (SSI) program from the Federal Government. The fees charged by the Federal Government to the Commonwealth and its program recipients to administer this program have been increasing for the past several years, and I believe we could do a more cost-effective job managing this program. I hope and expect that the Legislature will give this initiative very serious consideration and their support.

In Fiscal Year 1998, we proposed \$10 million in additional spending to reduce the waiting list for day and residential services provided by the Department of Mental Retardation (DMR). The Legislature appropriated \$5.75 million. This year, I am recommending a \$7.55 million increase in state spending to reduce the DMR waiting list, and hope the Legislature will see fit to approve a similar amount. I am also seeking \$4.4 million for services for persons with mental retardation who are turning 22.

Finally, I am requesting a \$3.5 million increase in state spending to support vocational rehabilitation, supported employment, independent living, and interpreter services at the Massachusetts Rehabilitation Commission, the Massachusetts Commission for the Blind, and the Massachusetts Commission for the Deaf and Hard of Hearing.

Public Safety

Over the past few years, our efforts to toughen sentencing guidelines and reduce early release and parole have helped state and local law enforcement officials secure a dramatic drop in virtually every type of crime. Simply put, criminals who stay in prison do not commit crimes. Our success in keeping criminals off the streets has resulted in a difficult, but manageable, over-crowding problem in our correctional facilities. To remedy this situation, we will be opening a brand new 1,000 bed maximum security prison in Shirley this fall. This state-of-the-art facility should provide the Commonwealth with a tremendous resource for years to come. I am recommending \$25 million in new state funds to support the opening and operation of this facility in Fiscal Year 1999.

I am also recommending that all parolees be required to pay for at least part of the cost of administering parole activities. In particular, I am recommending that each parolee be charged between \$25 and \$100 per month, and that the funds generated by these fees be used to expand and standardize drug testing procedures and protocols.

An additional \$2 million is also being recommended to fund Community Policing programs. These programs have proven an effective measure in our fight against crime, and deserve additional state support.

The District Attorneys will receive an 8% increase in our budget proposal, increasing state support for their efforts from \$65 million to \$70 million. I am also recommending \$13 million to conclude the Juvenile Court system expansion, and I am fully funding the Committee for Public Counsel Services. I am also providing \$1.5 million for expansion of legal assistance and advocacy for domestic violence victims, and expansion of the teen dating violence prevention program.

Finally, I am recommending another \$5 million to purchase State Police cruisers. Since Fiscal Year 1993, the Commonwealth has purchased over 2,000 new cruisers, turning over virtually the entire fleet of vehicles. Another \$5 million in Fiscal Year 1999 will make it possible for the State Police to purchase about 225 vehicles.

Environmental Affairs

Over the past 12 months, Massachusetts has moved aggressively to do a better job of coordinating and improving the quality of the monitoring and protection of its watersheds. To support these efforts and to provide a consolidated database of information for all those involved in monitoring watersheds, I am recommending a three-part approach. First, I am recommending \$600,000 to establish a Science and Technology Center to support all water quality monitoring efforts in general, and the Water Basin Protection initiative in particular. Second, I am recommending almost \$1 million to support outreach efforts, training programs, and grants to local water protection and water quality monitoring organizations. A comprehensive, collaborative effort between state, local communities, and regional experts is the most cost-effective way of monitoring watersheds, and needs to be pursued. Finally, I am including \$300,000 to establish, on a demonstration basis, a water pollution credit trading program, similar to the programs already in place concerning air pollution. If successful, such an initiative could dramatically enhance private sector performance on water emissions activities.

In addition, to help us mark the centennial anniversary of our Massachusetts State Park system in 1998, I am including \$2 million for additional park rangers, better informational materials and maps, and maintenance improvements. We have increased spending for state parks by 30% over the past five fiscal years.

Cities and Towns

For the fourth year in a row, the Commonwealth will continue to reduce its reliance on existing Lottery proceeds, and will dedicate any new growth in Lottery revenues to the Commonwealth's cities and towns. This practice will add a minimum of \$34 million in Lottery proceeds for cities and towns in Fiscal Year 1999.

State support for school building assistance continues to grow. This budget recommends a \$25 million increase in state support for the School Building Assistance Bureau (SBAB) program, which will fund 59 new school construction projects. In Fiscal Year 1991, the

Commonwealth appropriated \$128 million to support the SBAB program. The Fiscal Year 1999 request is \$237 million, an 85% increase in eight years.

For the sixth year in a row, the Commonwealth will fund a water and sewer rate relief program. Previous efforts have dedicated over \$200 million in state funds to the Massachusetts Water Resources Authority and other local water and sewer authorities to offset the burden on cities and towns. This year's recommendation is \$55 million, which is \$5 million higher than previous appropriations. This is due to the incorporation of debt service associated with the MetroWest Water Tunnel into the Commonwealth's rate relief program. I will continue to pursue every opportunity to reduce the growth in water and sewer bills. Ratepayers deserve clean water. They do not deserve to get soaked.

I am also including state funds to support local drinking water projects: \$8 million in contract assistance for existing projects and another \$2 million to support low-interest loans for new projects; and \$31 million in contract assistance for clean water projects, an increase of \$4 million.

Finally, I am including \$1.4 million to support the Innercity Bus Purchase program. This program will enhance the availability of transportation for residents of communities not served by the MBTA.

The Math

House 1A calls for spending \$19.06 billion in Fiscal Year 1999. Policy decisions to protect state and federal funding for the Health Care Access Act of 1996, along with several other minor transfers, have reduced budgeted Fiscal Year 1999 spending by more than \$400 million. Total spending, including off-budget transfers, represents a 3.4% increase over anticipated Fiscal Year 1998 spending. The vast majority of this increase - \$540 million - supports full implementation of the Health Care Access Act and aid to cities and towns. The rest of state government is projected to grow by \$100 million, or less than 1%.

Tax and departmental revenue assumptions under this proposal are very conservative. This budget assumes base tax revenue growth in Fiscal Year 1998 of 5.2%, and base tax revenue growth in Fiscal Year 1999 of 4.9%. Each of these estimates is below projections issued earlier this year by the Massachusetts Taxpayers Foundation. Consistent with our commitment to fiscal discipline, we choose to begin the budget deliberation process with a realistic revenue estimate that may prove to be too low rather than assuming the risk of being forced to adjust an overly optimistic revenue estimate downward later on.

Looking Ahead

For the past seven years, this Administration has worked cooperatively with the Legislature to right the Commonwealth's fiscal ship of state. We have succeeded. While the

Commonwealth's fiscal health has never been better, we owe the citizens of the Commonwealth a pledge of constant vigilance to ensure that our fiscal recovery not only succeeds but endures. Even a cursory review of budget documents and press releases from the mid-1980's reminds us that the sounding of similar themes of prosperity can become a siren's call culminating in the type of unfortunate downturn that our economy experienced in the late 1980's and early 1990's.

We will not make the same mistakes that were made during the 1980's. Our spending proposals are restrained, our tax and departmental revenue estimates are conservative, and our commitment to fiscal prudence has, quite simply, never been stronger. The Commonwealth's capacity to fund education reform, expand health care coverage, reduce our unfunded pension liability, and fund programs that fight domestic violence, AIDS, and juvenile crime are built on one fundamental principle: a government that cannot cut its own taxes and balance its own budget cannot truly help anyone.

I look forward to this opportunity to work with the Legislature to craft a budget document for Fiscal Year 1999 that is restrained, balanced, and further reduces the tax burden that our citizens continue to bear on both earned and unearned income.

